

Low-Income Housing Tax Credits

- **In General**

The 1986 Tax Reform Act created the low-income housing tax credit (the "Tax Credit"), under §42 of the Internal Revenue Code of 1986, as amended (together with Treasury *Regulations* promulgated thereunder, the "Code"), to encourage the private sector to invest in the construction and rehabilitation of housing for low and moderate income individuals and families by providing qualified owners with credits against their federal income tax obligations. The Mayor has designated the Department of Housing and Community Development (the "Department") as the agency authorized to allocate Tax Credit for residential rental projects in Washington, DC under this program (the "Tax Credit Program"). The Director of the Department (the "Director") has assigned this function to the Development Finance Division, a Division of the Department of Housing and Community Development ("DHCD"). The Tax Credits are available to *owners of qualifying* residential rental projects that meet certain low-income occupancy and rent restrictions.

Generally, each state is allocated a specified amount of Tax Credits annually, based primarily on the state's population. In addition, states that allocate 100% of their annual authority are eligible for additional authority for the following year from a national pool of unused Tax Credit authority.

- **Determining the Amount of Tax Credit**

The Tax Credits are generally provided to project owners in equal annual installments over a 10-year period. The Tax Credits may not exceed the applicable percentage of the qualified basis of each low income building in the project as defined in section 42(d) of the Code. The applicable percentage is the percentage that will yield over the 10 year Tax Credit period, Tax Credits with a present value equal to either 70% or 30% of the qualified basis of the building. New construction and rehabilitation projects that are not federally subsidized are eligible for the 70% present value Tax Credit. Projects financed with federal funds or involving the acquisition of existing buildings (when combined with eligible rehabilitation) are eligible for the 30% present value Tax Credit. The Code also requires administering agencies to allocate only the amount necessary to make developments feasible. DHCD will make this determination at three points in the process: at the time of application; at the time of reservation; and at the time the building is placed in service.

- **Income and Rent Restrictions**

The owner must elect to set aside, at a minimum, either 20% of the housing units in the project for households with incomes of 50% or less of the area median gross income, or 40% of the housing units in the project for households with incomes of 60% or less of the area median gross income. Household size is based on certain assumptions involving the bedroom configurations of the rental units. Rents for Tax Credit units may not exceed 30% of the applicable income limit.

The housing units must set aside for low-income residents for an initial compliance period of 15 years (the "Initial Compliance Period"). In addition, federal law requires the owner to enter into an Extended Low-Income Housing Covenant (Extended Use Covenant) with DHCD under which the low-income housing set-aside (meaning the actual number of units that general Tax Credits and are set aside for low-income tenants), the rent restriction, and other requirements must continue for an additional period of at least 15 years beyond the Initial Compliance Period (together, the "Extended Use Period"). The Code permits an owner to opt-out of the program restrictions after 15 years under certain circumstances. However, in order to score additional points in the rating and ranking

process (see Allocation Criteria" below), a project owner must agree to an extended Use Period of at least 40 years.

Proposed Allocation Plan Overview

- **Introduction**

The Code requires states to adopt a plan (the "Allocation Plan") to allocate the Tax Credits to projects based on state priorities and federally mandated requirements. This Allocation Plan is intended to ensure that only projects that comply with federal law and address the housing priorities of Washington, DC are selected for an allocation of Tax Credits. The Allocation Plan will set forth DHCD's selection criteria for use in determining housing priorities for allocating Tax Credits.

Award of Tax Credits

Tax Credits are awarded to eligible housing projects on a competitive basis and are limited under the Code to an annual ceiling amount. One or more competitive rounds are held each year, awards are based on the criteria outlines in this allocation plan (see "Allocation Criteria" below) and in DHCD's Financing Program Guide (the "Program Guide"), attached to and made a part of this Allocation Plan as Appendix A. The allocation criteria and the competitive process apply to residential rental projects other than those financed by tax-exempt bonds. Projects financed with certain tax-exempt bonds may be eligible to receive all or some of their Tax Credits outside the District's ceiling. Although these projects need not compete for an award through the competitive process, they must still be evaluated against the threshold criteria and the project selection criteria and must comply with the provisions of the Allocation Plan.

The Program Guide describes in detail DHCD's criteria requirements, and policies for evaluating, ranking, and selecting projects for Tax Credits, making Tax Credit reservations and allocations, and administering the Tax Credit Program.

The determination of whether a Project will receive an allocation of Tax Credits rests solely with DHCD and is contingent upon owners compliance with §42 of the Tax Credit Program, which may be more restrictive than the requirements of §42 of the Code.

Adoption of the Allocation Plan

Before Adopting the Allocation Plan, including the Program Guide, DHCD will hold a public hearing after giving at least 14 days notice to the public by means of publication in a number of newspapers of general circulation. Public comments were permitted in writing at the office of DHCD any time up to the beginning of the public hearing, and verbal comments were received by DHCD at the public hearing. The Allocation Plan, including the Program Guide, will be submitted to the Mayor for approval.

Application Process and Fees

Application for Tax Credits will be solicited by DHCD by public notice in one or more competitive rounds during the year. For a project to be considered for an allocation of Tax Credits, DHCD must receive a completed application, together with a non-refundable application fee, within the deadline specified in the public notice. To be evaluated during any round of competition (the competition is referred to as "rating and ranking"), projects must meet all of the threshold criteria specified in the Program Guide. These requirements are intended to

eliminate projects that do not meet basic program requirements and to ensure that Tax Credits are reserved for projects that meet federal requirements are both viable and ready to precede. Projects that do not meet the threshold criteria will not be rated and ranked during competitive rounds.

Fees

Application Fee. All sponsors must pay a nonrefundable fee of \$1,000 for each application requesting a reservation of Tax Credits. If the sponsor is also applying for multifamily rental housing funds, the sponsor shall pay a combined application fee of \$1,000 for both programs. This fee must be paid at the time the application is submitted and retained by DHCD whether or not the application is successful. Projects failing to receive an award of Tax Credits may reapply in another year, but a new application fee will be required.

Reservation Fee. All sponsors must pay a nonrefundable reservation fee. Failure to pay the reservation fee, in the amount and at the time required as set forth below, will result in the cancellation of the reservation. DHCD will not issue an allocation of Tax Credits or an IRS Form 8609 needed to claim the Tax Credits unless all reservation fees have been paid.

Allocated Credits:

Profit-Motivated Sponsors. Profit-motivated sponsors must pay a nonrefundable reservation fee equal to 2% of the annual Tax Credits reserved for the project upon the earlier of the filing of a binding agreement and election statement or the date the project is placed in service.

Nonprofit Sponsors. Non Profit sponsors must pay a fee of \$1,000 upon the filing of a binding agreement and election statement. When the project is placed in service, nonprofit sponsors must pay an additional fee equal to 2% of the annual Tax Credits allocated to the project, less the \$1,000 reservation fee previously paid.

Tax-Exempt Bond Financed Projects:

Projects that have 50% or more of the development and acquisition cost financed with the proceeds of tax-exempt bonds may receive Tax Credits on their entire basis outside the District's tax credit ceiling. Projects with less than 50% of their cost financed with the proceeds of tax-exempt bonds may receive Tax Credits on the portion of the cost so financed without requiring an allocation. Sponsors interested in pursuing Tax Credits with tax-exempt bond financing should contact the District of Columbia's Housing Finance Agency.

Extensions

Extension of Reservation. Sponsors unable to meet the requirements to receive an allocation of Tax Credits within the period specified in their reservations may request an extension of the reservation. All sponsors must pay a non-refundable extension fee of \$1,000 for each project for which an extension of the reservation is requested. The fee must be paid at the time the extension request is submitted.

Extension of Time to Satisfy Requirements for Carryover Allocation. Sponsors unable to meet the deadline for meeting the requirements for a carryover allocation (see "Allocations" below) may request an extension of the deadline for one month. All sponsors must pay a nonrefundable extension fee of \$1,000 for each project for which an extension of time to meet this deadline is requested. The fee must be paid at the time the extension request is submitted.

Extension of Reservations or Carryover Allocation cannot be granted for deadlines applicable under §42 of the Code and sponsors are responsible for understanding and meeting all such deadlines.

Reservations

In General

Except for set-asides for Director's Reserve, applications will be evaluated based on the rating and ranking of the projects using the evaluation criteria set for in detail in the Program Guide. Recommendation for reservations of *Tax Credits* will be made by DHCD's to the Loan Review Committee ("LRC"). After evaluating DHCD's recommendations, LRC will make a final recommendation to the Director, who must approve each reservation of Tax Credits. After application have been evaluated against the threshold criteria and rated and ranked, the Director may approve reservations of Tax Credits without recommendation by LRC in emergencies or when urgent action is required. If, in any round of competition, DHCD determines in its sole discretion that the submitted projects have low compliance with project selection criteria, DHCD reserves the right not to make any recommendations for reservations of Tax Credits at that time and to evaluate the applications in a subsequent round.

In general, for projects competing in any round of rating and ranking with awards made before July 1 of any calendar year, following recommendation LRC and approval by the Director, DHCD will issue a reservation letter to the sponsor. This reservation letter is a commitment to reserve Tax Credits for the project, subject to receipt of documentation indicating timely completion of the project, certifying compliance with state and federal requirements, verifying project cost (at the time of allocation and at the time the project is placed in service), and showing the amount of Tax Credits necessary for the financial feasibility of the projects and its viability as a low income housing project.

For projects competing in any round of rating and ranking with awards made after June 30, allocations, not reservations, will be issued by DHCD after recommendation by LRC and approval by the Director. Develop a section on Allocations for more information.

In the event that reservation of Tax Credits are approved or denied on any basis other than an application's evaluation against the threshold criteria and its rating and ranking under the evaluation criteria or its evaluation under the Director's Reserve (described below), DHCD will include in the application file, and make available upon public request, a written explanation of the approval or denial of Tax Credits, as applicable.

Forward Reservations

Under certain conditions a project may be eligible to receive a reservation of Tax Credits from the District's ceiling for future years (a "Forward Reservation"). To receive a Forward Reservation, project sponsors must agree to comply with all conditions imposed by DHCD and the IRS. The following types of projects may receive Forward Reservation from a future year's Tax Credit ceiling:

Projects Unable to Meet Deadlines. DHCD may approve Forward Reservation or project that have already received reservation letters but are not able to be placed in service in the year of their reservation or unable to meet the 10% expenditure test as provided in the Internal Revenue Code §42(h)(1)(E). Such projects must be considered for a Forward Reservation only if the Tax Credits reserved can be allocated to other project or be carried forward for allocation in a future year. To be considered for a reservation extension, sponsors must remit a \$1,000 non-refundable extension fee.

DHCD may approve a Forward Reservation for projects that ranked high enough in a round of competition for an award of Tax Credits but for which there insufficient remaining Tax Credits that can be allocated in the current year.

Multiple Year Reservations. DHCD may approve a Forward Reservation when projects or reservation will be appropriately staged over two or more years. DHCD will determine if the sponsor's request for Tax Credits is large enough to limit the available resources in the current or future years for other projects that otherwise qualify for a reservation.

Increases of Reservations

DHCD may approve increase in the amount of Tax Credits reserved for project of up to 10% of the amount previously approved by the Secretary. Such increases may be approved only from the time the reservation letter is issued until the time a Carryover Allocation is issued. Projects whose Tax Credits are increased after approval by the Director need not be re-evaluated against the threshold and project selection criteria. The aggregate increases approved by DHCD may not exceed 10% of the District's Tax Credit ceiling for the year of the increase.